

Agenda Date: October 26, 2005  
Item Number: A5 and A6

**Docket:** **UG-051480 and UG-051483**  
Company: Cascade Natural Gas Corporation

Staff: Joanna Huang, Regulatory Analyst  
Yohannes Mariam, Regulatory Analyst

**Recommendation:**

Take no action, thereby allowing the tariff sheets filed in Dockets UG-051480 and UG-051483 to become effective on November 1, 2005, as filed.

**Background:**

On September 29, 2005, Cascade Natural Gas Corporation (Cascade) filed its Purchase Gas Adjustment (PGA) and Deferred Gas Cost Amortization tariffs in Dockets UG-051480 and UG-051483, respectively. The combined effect of the two filings is an increase in annual revenues of \$48,741,527 (26.3%).

Cascade serves approximately 163,600 gas customers in various areas situated primarily along Williams Gas Pipeline. Major Washington locations include Bellingham, Bremerton, Yakima, and Walla Walla.

The PGA and Deferral Amortization mechanisms are designed to pass on actual gas costs to customers. The PGA establishes for the upcoming year what the best projection is going to be for the cost of gas. The difference between the projected cost and the actual cost is deferred and amortized back to customers with interest.

**Purchase Gas Adjustment (PGA):**

Docket UG-051480 is the proposed PGA filing. In this filing, Cascade presents data and methods used in the determination of prospective gas cost for the coming year. The Company is proposing an increase of approximately \$44.1 million (23.82%) in annual revenue for this filing. Cascade is proposing a weighted cost of gas of \$0.8787/therm (commodity \$0.77776, firm demand \$0.10094) in this filing.

### **Concerns Regarding Cascade's Hedging Strategy:**

Staff is concerned about Cascade's natural gas purchasing strategy. Cascade entered into three-year contracts at high gas prices without making a detailed analysis about market fundamentals and the longevity of the impact of Katrina on future deliveries and prices. While this may not adversely affect the cost of gas for the coming year, Staff is concerned that it unduly limits Cascade's ability to respond to market changes in subsequent years. Cascade's hedging strategy does not follow recommendations contained in the Commission's acknowledgement letter of the company's most recent least cost plan dated June 22, 2005. The letter states:

"The choice between fixed price contract, financial derivatives, and other instruments should be based on some protocol to minimize risk-weighted gas costs. The IRP discussed the percentage of the gas supply to hedge and when it should be hedged. However, it did not specify whether or not that percentage and timing was the results of the optimization routine or judgment. The Commission encourages Cascade to use sound empirical analysis as well as professional judgment to make these determinations. Cascade's approach should also be flexible enough to take advantage of low price swings and limit the consequences of high price excursions."

Accordingly, Staff advises the company that its future hedging practice should rely on sound and thorough analysis of fundamentals and market information and retains greater flexibility to respond to market changes, especially when gas costs are expected to decline.

### **Gas Cost Deferral Amortization**

Docket UG-051483 is the gas cost deferral amortization filing. This filing is designed to pass on actual gas costs to customers. The difference between the projected gas cost and the actual gas cost is deferred and amortized back to customers with interest, whether it is a refund or surcharge. The tariff sheet results in an increase to annual revenues of \$4.7 million (2.51%).

Summary:

The impact of the two filings on a monthly bill to residential customers with consumption of 57 therms will be an increase of \$14.20 (25.14%).

The combined effects of the PGA and deferral amortization on the Company's rates (\$/therm) and annual Washington revenues are as follows:

	PGA <u>Change</u>	Deferral <u>Change</u>	Revenue <u>Impact</u>	Percent <u>Change</u>
Residential	\$ .22570	.02361	\$24,932,494	25.14%
Commercial	.22556	.02361	19,856,425	27.48%
Industrial-firm	.22484	.02361	2,810,168	29.04%
Interruptible	.22412	.02361	1,104,629	34.08%
Non-Core		.00508	<u>37,812</u>	<u>5.24%</u>
Total			<u>\$48,741,528</u>	<u>26.30%</u>

Conclusion:

Staff has reviewed the Company's prospective gas costs and deferral accounts. Staff recommends the Commission allow the filings in Dockets UG-051480 and UG-051483 to become effective November 1, 2005, as filed.